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# Newly Industrializing Countries' Export Assistance Programs: A Growing Challenge

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A Research Paper

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# Newly Industrializing Countries' Export Assistance Programs: A Growing Challenge [redacted]

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**A Research Paper**

This paper was prepared by [redacted] Office of Global Issues. Comments and queries are welcome and should be directed to the Chief, Third World Issues, Economics Division, OGI, [redacted]

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# Newly Industrializing Countries' Export Assistance Programs: A Growing Challenge

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**Summary**

*Information available as of 6 July 1983 was used in this report.*

The newly industrializing countries (NICs) have established sophisticated export assistance programs, which rival similar programs in industrial countries. Brazil and Mexico do the most to promote exports, closely followed by South Korea and Taiwan. Singapore has recently introduced some export promotion measures to counter the effects of the global recession, while Hong Kong retains its laissez faire trade policy. We have no way of gauging how much government assistance has contributed to the rapid growth of NIC-manufactured exports, but, based on a review of the programs, at least one-half of these exports benefit from some form of tax or financial incentive. 25X1

NIC industrial development plans and export assistance programs suggest that the NICs are successfully adjusting their trade policies to support their industrial goals by:

- Trying to shift their export-oriented industries away from traditional "cheap labor" products—textiles, apparel, and consumer electronics—toward manufactured goods that use more capital, skills, and technology—machine tools, precision equipment, computers, and computer-related equipment.

- Stepping up their use of certain export incentives—particularly officially supported credits—and concentrating them on the industries targeted for development. 25X1

We expect further changes in both the types of export incentives the NICs offer and the industries they promote. US businessmen and bankers think the NICs probably will try to trim the cost of export financing by reducing direct loans to overseas buyers, which require substantial government support, in favor of interest rate equalization programs, which involve a transfer of funds equal to the difference between the lender's cost of obtaining the funds and the preferential rate charged to the borrower. Judging by their industrial plans, we anticipate that South Korea, Taiwan, and Singapore will begin targeting more export assistance to the shipbuilding, machinery, and electronics industries—including avionics and other semi-high-technology sectors. By contrast, Mexico and, to a lesser extent, Brazil will probably continue to focus on the steel, transport equipment, textile, and apparel industries because their international payments problems are likely to preclude much restructuring of their industries. 25X1

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The NICs are formidable competitors in certain product lines in the United States, and we believe their export assistance programs enable them to capitalize on US economic recovery by taking larger market shares of such consumer goods as clothing and footwear and such industrial goods as electrical machinery. In the medium term, we see NIC competition shifting to higher technology products. While the NICs almost certainly will not export across the board in high-technology goods, we believe they will locate market niches that can be promoted by their export incentive programs and exploited on the basis of price. 25X1

Targeting of markets will have a dual impact on the West. Many of the tensions between the NICs and the industrial countries over labor-intensive goods will shift to new products. At the same time, the growing technical sophistication of the NICs' output gives them the potential to become alternative suppliers to the Soviets. If Western sales opportunities were curtailed or if Soviet Bloc trade were to become more lucrative, little would prohibit the NICs from expanding trade with the East. Any pressure to sell to the Soviets and their surrogates will be even more intensive in NICs, such as Mexico and Brazil, that are financially strapped. 25X1

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**Table 1**
**Newly Industrializing Countries:**
**Penetration of Selected US Manufactured Goods Markets**

| Imports From NICs | Total | Clothing | Leather and Footwear | Wood and Cork Manufactures | Electrical Machinery | Textiles | Metal Goods | Rubber Goods | Nonelectrical Machinery |
|---|---|---|---|---|---|---|---|---|---|
| **1970** | | | | | | | | | |
| Value (*million US $*) | 2,192 | 572 | 85 | 149 | 441 | 104 | 51 | 2 | 56 |
| Share of total imports (*percent*) | 9.1 | 45.2 | 11.4 | 36.0 | 19.9 | 9.2 | 6.2 | 1.0 | 2.5 |
| Share of total consumption (*percent*) | 0.5 | 2.8 | 1.5 | 1.3 | 0.9 | 0.4 | 0.1 | NEGL | 0.1 |
| **1981** | | | | | | | | | |
| Value (*million US $*) | 26,947 | 5,349 | 2,101 | 573 | 6,577 | 688 | 1,142 | 237 | 1,716 |
| Share of total imports (*percent*) | 19.1 | 65.9 | 55.1 | 40.7 | 37.4 | 22.4 | 26.0 | 14.2 | 10.2 |
| Share of consumption in 1979 (*percent*) | 1.3 | 10.1 | 12.6 | 1.9 | 4.0 | 0.8 | 0.8 | 1.0 | 0.6 |

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# Newly Industrializing Countries' Export Assistance Programs: A Growing Challenge [redacted]

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## Introduction

Brazil, Hong Kong, Mexico, Singapore, South Korea, and Taiwan have moved rapidly toward becoming relatively industrialized. Under strategies of export-led growth, these newly industrializing countries (NICs) experienced average annual real GDP growth of over 7 percent during 1965-82, far more than the 4-percent growth registered by the OECD for the same period. Moreover, the NICs' rapid emergence as exporters of manufactured goods has led to increased penetration of US and other industrial-country markets for selected products. Although the NICs have only a small share of the US-manufactured goods market, they have captured a large share of US imports in certain product lines (table 1). Moreover, the NICs' market penetration has occurred during a period of slow world growth and high unemployment. As a result, industrial countries have been sensitive to the NIC challenge. [redacted]

To maintain the dynamic growth they achieved over the past 15 years, the NICs have been adjusting the focus of their export strategies. They have shifted the structure of their export-related industries away from traditional "cheap labor" commodities toward the production of more sophisticated products that use substantial inputs of capital, skills, and technology. An earlier study of the industrial plans for each country indicated that the industries targeted for development include machine tools, microelectronics, transportation equipment, telecommunications equipment, minicomputers and microcomputers, and financial and information services.[1] [redacted]

According to plans described in both press and official NIC reports, the policy tools chosen by the NIC governments to push development of these industries fall into three broad categories: domestic demand management, incentives for industrial development, and export promotion. This paper examines the export assistance programs used by the NICs, how they are being changed to promote the export of more sophisticated manufactured products, and the challenges they pose. [redacted] 25X1

## Export Assistance

***National Strategies.*** Under the development strategies pursued by the NICs, trade is a driving force of economic growth. The importance attached to trade is clearest in the cases of South Korea, Taiwan, Hong Kong, and Singapore. With ratios of exports and imports to GNP in 1981 of 87 percent, 105 percent, 152 percent, and 172 percent, respectively, these countries virtually live by trade. For the United States, this ratio was only 20 percent. [redacted] 25X1

Our survey suggests that the governments of Brazil and Mexico are doing the most to promote exports and Hong Kong and Singapore the least.[2] Although NIC programs vary in size and content (table 2), their main objectives are to increase the profitability of manufactured goods to encourage domestic firms to produce them and to lower the export prices of these goods to ensure that they are competitive in world markets. These goals are accomplished through such broad-based measures as exchange rate policies and more narrowly focused policies such as tax and duty concessions, preferential credits, government promotion and marketing, and an array of other measures such as trading companies and free trade zones. [redacted]

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*Brazil* uses practically all of the known policy tools to promote exports, including restrictions on imports that compete with potential Brazilian exports, but relies mainly on tax incentives and official export financing. In its recent arrangement with the IMF, Brasilia agreed to shift away from product-specific incentives to incentives that improve the price competitiveness of all exported manufactured goods and

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[2] A detailed discussion of the specific export promotion measures used by each NIC is available in appendix A. [redacted] 25X1

[redacted]

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**Table 2**
**Newly Industrializing Countries: Summary of Export Promotion Measures**

| | Brazil | Hong Kong | Mexico | Singapore | South Korea | Taiwan |
|---|---|---|---|---|---|---|
| Exchange rate policy | Devaluation of cruzeiro in line with the domestic rate of inflation. | No foreign exchange restrictions. | Two-tier exchange rate regime. | No foreign exchange restrictions. | No significant foreign exchange regulations. | No restrictive measures affecting trade transactions. |
| Import restrictions | Tariff and nontariff barriers to protect industry and stem widening balance-of-payments deficit. | Imports are virtually free of restrictions. | Fairly restrictive import duties and licenses. | Almost all imports enter freely. | Has initiated a major import liberalization program. | Import restrictions have been gradually reduced.<br><br>Customs tariffs are main instrument of control. |
| Fiscal incentives | Incentives to exporting firms:<br>— Exemption from value-added taxes.<br>— Value-added tax credits.<br>— Export-related income tax reduction.<br><br>Incentives for export production:<br>— Duty and tax breaks on imported inputs.<br>— Duty drawback system. | Flat 17-percent gross profit tax.<br><br>No protective tariffs, capital gains tax, or corporate income tax. | Tax rebate on imported machinery used in production of exports.<br><br>Duty-free import of materials used in exports that are nôt available domestically. | Exemption of corporate income tax for specific export-oriented "pioneer" industries.<br><br>Reduction in corporate income taxes for firms exporting nontraditional products.<br><br>Double deduction of export promotion expenses. | Tariff rebate system.<br><br>Reduction in corporate taxes for exported goods and expenses for producing and marketing exports. | Business tax exemption on export sales.<br><br>Tax rebate on imports of raw materials used in exported products.<br><br>Duty exemption for selected imports of machinery and equipment. |
| Financial incentives | Interest rate equalization export financing.<br><br>Working capital loans. | No subsidies or supported funding programs. | Export and preexport financing through a discounting facility. | Interest rate equalization facility.<br><br>Export bill rediscounting scheme.<br><br>Preferential financial assistance for domestic shipbuilding. | Preferential short-term export financing.<br><br>Provision of direct medium- and long-term buyer and supplier credits via Korea Export-Import Bank. | The Export-Import Bank of China directly finances buyer and supplier credits.<br><br>Refinancing through the Fixed Rate Relending Facility. |

| | | | | | | |
|---|---|---|---|---|---|---|
| Government promotion | Sponsors trade fairs.<br><br>Marketing research and other promotions. | Trade fairs.<br><br>Industrial promotion offices.<br><br>Four trade journals. | Overseas export promotion offices.<br><br>Marketing research.<br><br>Training for executives. | Conducts trade fairs; otherwise, prefers each firm to promote own exports. | Trade fairs and exhibits.<br><br>A variety of market development programs. | Streamline trade administration procedures.<br><br>Sponsors trade fairs and provides facilities for export exhibits.<br><br>"Buy American" and "Buy European" programs. |
| Other measures | Export finance insurance.<br><br>Promotion of trading companies.<br><br>Operation of six free trade zones. | Export finance insurance. | Export finance insurance.<br><br>Export finance guarantees.<br><br>Free trade zones. | Export finance insurance.<br><br>Export finance guarantees. | Export finance insurance.<br><br>Export finance guarantees.<br><br>General trading companies.<br><br>Two free trade zones. | Export finance insurance.<br><br>Export finance guarantees.<br><br>Three export processing zones. |
| Comments | Recently imposed IMF austerity measures improve price competitiveness of exports. Underlying incentive system will continue to promote traditional manufacturing subsectors. | Laissez faire trade policy. | Under pressure from major trading partners, has suspended tax credits for exporters. IMF austerity program aims to enhance export competitiveness by liberalizing import regime and providing more equitable distribution of export subsidies. | Generally avoids direct export incentives. However, recently introduced tax and financial packages favor capital-intensive exports. | Fifth Five-Year Plan for 1982-86 signals change from detailed quantitative export targets to policies that allow market forces to operate more freely, subject to some government regulation and protection. | Objective of trade policy is to diversify international trade by widening export lines and expanding trade with new partner countries. |

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increase export earnings. Because of its pressing foreign exchange needs, the government of Brazil's long-term industrial ideology has yielded to short-term pragmatism.

Since 1979, *Mexico*'s export promotion program has concentrated on industries selected by the government as potentially competitive—mining, textiles, steel, automobiles, capital goods, chemicals, metal products, rubber, and petrochemicals. To promote the development and exports of these industries, Mexico developed a complex system of import duties and licenses, tax and duty rebates on machinery and raw materials used in the production of exports, as well as export and preexport financing. According to the IMF, these measures have been uncoordinated, resulting in wide disparities in the incentives granted to different industries. Because of its recent serious financial crisis, the government of Mexico announced in mid-May a new export development plan. Outlined in its letter of understanding to the IMF on 7 January 1983, the Mexican Government agreed to certain changes in the tariff structure, tax incentives, and import licensing requirements. These revisions are intended to enhance the competitiveness of Mexico's less favored export industries—such as mining—and to reduce subsidies to industries primarily in the manufacturing sector that have received what the IMF considers an inordinate amount of support.

Last year *South Korea* deemphasized its practice of closely managing both exports and imports in favor of policies designed to strengthen the competitiveness of exports in general. Seoul has not abandoned regulation and protection of exporting sectors of the economy, but it no longer sets specific export and import targets, which frequently required manipulation of tax and financial incentives. The government has liberalized import licensing, reduced some tariffs on goods imported by exporters, and begun to phase out short-term preferential export credits.

A major objective of *Taiwan*'s trade policy is to diversify export product lines and expand trade with countries other than the United States and Japan. Although Taipei endorses freer trade, it provides a variety of economic incentives to exporters. Manufacturers are exempted from the business tax on their export sales and from duties on the imported raw materials and machinery used in exported products. The Export-Import Bank of China offers direct supplier and buyer credits as well as below-market fixed-rate relending facilities for the export of capital goods. 25X1
In providing these credits, government planners seek to move domestic manufacturers toward the production and export of such higher technology and higher value-added goods as transport equipment, machinery, electrical and electronic equipment, precision instruments, and basic metals. 25X1

*Hong Kong* maintains a laissez faire stance toward trade policy. There are no export subsidies or tariffs and a minimum of trade restrictions. Government participation in trade promotion is principally in the form of export finance insurance, trade fairs, and industrial promotion offices. 25X1

*Singapore,* like Hong Kong, has generally left local firms to promote their own exports. According to diplomatic reporting, however, Singapore has modified its policies in the face of rising international protectionism and a decline in the competitiveness of its traditional exports. To expand into higher value-added exports, the government now offers tax breaks to firms that export nontraditional products and is providing concessional export financing to promote capital-intensive industries. Only a select group of higher technology industries such as aircraft components, electrical tools, and microwave equipment qualify for the tax relief incentives. 25X1 25X1

**The Changing Focus of Export Incentives**

Our examination of the NICs' export assistance programs suggests that two types of changes have been occurring as NIC governments try to export more sophisticated products and cope with growing competition for world markets. We believe the NICs are using a broader mix of measures to promote exports, and that these incentives are being increasingly concentrated on specific manufacturing subsectors such as compressors, measuring devices, and photographic and optical instruments. 25X1 25X1


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***Measures Used.*** After employing outward-looking growth strategies in the mid-1960s, the NICs implemented programs that were built around import restrictions, fiscal incentives, exchange rate policy, and free trade zones to promote the production and export of their manufactured goods. Today, these instruments are complemented by financial incentives, the operation of general trading companies, and aggressive government promotion. [redacted]

One of the more noteworthy developments in the NICs' export assistance programs is the relatively recent emergence of *officially supported export credits*. Since the mid-1970s, each of the NICs except Hong Kong has established a preferential financing facility to soften the terms of export financing and enhance the competitiveness of its exports. Moreover, each NIC provides some form of export insurance or guarantee to protect domestic producers against the commercial and political risks encountered when extending credit to foreign buyers of their manufactured goods. [redacted]

The NICs' financing facilities are comparable in most respects to those of industrial countries (table 3). They operate several types of direct funding, interest rate equalization, and refinancing programs.[3] One basic difference, however, is that the NICs provide assistance to export transactions with credit terms of less than six months; industrial country governments require two years and longer. [redacted] Brazil and Mexico have the most extensive export credit programs with respect to financial outlays and product coverage. These are followed by South Korea and then Singapore and Taiwan. [redacted]

Although comprehensive data are not available on the volume of NIC export credits, some notion of their importance in promoting trade in manufactured goods can be gleaned from studies of Brazil's and Singapore's programs. The IMF calculates that credits extended under Brazil's interest rate equalization program rose from $700 million in 1976 to $1.7 billion in 1980. Data reported by the Monetary Authority of Singapore indicate that exports financed under Singapore's rediscounting scheme jumped from $36 million in 1975 to about $1.3 billion in 1981. As a share of total exports, these financed exports increased from 0.7 percent in 1975 to 6.2 percent in 1981. [redacted] 25X1

Because the NICs are beginning to enter markets in which they have limited product recognition, they are also emphasizing institutional ways to open up markets. South Korea, Brazil, and Taiwan already make fairly extensive use of *trading companies* to enhance financial resources and marketing expertise. This approach already seems to be paying off. In Brazil, for example, trading companies increased their share of total exports to 28 percent in 1982, up from 19 percent in 1981. [redacted] 25X1

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Each of the NICs has established some form of *official trade agency* to assist producers in marketing their manufactured goods. These agencies support the domestic producers by:

- Organizing seminars, conferences, and trade exhibitions to promote potential export lines. 25X1
- Locating potential buyers.
- Providing information and assistance to these buyers.
- Undertaking market research and related activities.

[redacted] 25X1

Although several NICs state that they intend to reduce their reliance on industrial country markets, we find little evidence to suggest that any of the NICs' economic incentives are designed specifically to promote exports to third-country markets. If the NICs were to use any of their economic incentives to discriminate between markets, we believe they would use official export financing schemes, which governments can readily direct toward favored buyers. We were unable to determine from the available data, however, the extent to which the NICs export credit agencies use the terms of these credits to promote the export of manufactured goods to selected markets. [redacted]

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[3] For a further description of these programs, see the glossary in appendix B [redacted]

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**Table 3**
**Newly Industrializing Countries: Comparison of Export Financing Schemes**

| Country | Type of Program | Administered by | Date Established | Repayment Period | Currency | Financed Portion (*percent*) | Domestic Content Requirement (*percent*) | Fee Consideration (*percent*) | Commitments in 1980 (*million US $*) | Comments |
|---|---|---|---|---|---|---|---|---|---|---|
| Brazil | Interest rate equalization | Bank of Brazil | NA | Six months to 10 years | US dollars | Less than two years, 100; two to 10 years, 85 | 80 | 7.5 to 10.0 | 1,700 | Devaluation of the cruzeiro reduced the dollar value to $800 million in 1982. |
| Hong Kong | None | None | None | None | None | None | None | None | None | None |
| Mexico | Rediscounting | Bank of Mexico | NA | 30 days to 10 years | US dollars and other approved currencies | Up to 100 percent of contract | 50 | 6.0 to 8.75 | 1,563 | Commitments include export and preexport financing. |
| Singapore | Interest rate equalization | Ministry of Finance & Export Credit Insurance Corp. | 1979 | Two to 10 years | Singapore dollars and US dollars | Up to 85 percent of Singapore content | None | S $10.125 to S $11.25 US $11.25 to US $11.625 | NA | Operation suspended. |
| | Rediscounting | Monetary Authority of Singapore | NA | Up to 180 days | Singapore dollars | Up to 100 | 30 | Generally rediscounted at 1.5 percent below the Singapore prime rate | 3,169 | Commitments refer to gross amount rediscounted. |
| South Korea | Buyer and supplier credits | Eximbank | 1976 | Two to 10 years | Korean won, US dollars, and other major currencies | 70 to 90 | Up to 75 | 9.0 to 10.0 | 403 | Commitments in 1979 were $928 million. |
| Taiwan | Buyer and supplier credits | Eximbank | 1979 | Two to seven years | US dollars | Up to 85 | 50 | 8.5 | 176 | Commitments include discounting offers and buyer and supplier credits. |
| | Relending | Eximbank | 1979 | Two to seven years | US dollars | Up to 90 | 50 | 8.5 | | |
| Japan | Buyer and supplier credits | Eximbank | 1950 | Two to 10 years | Japanese yen | Up to 55 | 50 | 9.25 | 3,900 | According to US bankers, Japan's export credit support is probably the broadest of industrial countries. |

All information as of 1981 unless otherwise indicated.

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### *The Question of Subsidies*

*Many developed as well as developing countries are concerned that the NICs may be supporting their exports excessively, thereby distorting international trade competition and causing economic harm to competing industries. To protect against this, the GATT has established a means of recourse to offset the economic effects of export subsidies and thus prevent injury to domestic industries. According to the US Special Trade Representative's Trade Action Monitoring System, since 1976 there have been 13 affirmative countervailing duty determinations against the NICs by the United States (see table 4). In most instances, the countervailing duties levied were on labor-intensive consumer goods that were subsidized through the use of fiscal incentives.* 25X1

*In addition to the GATT, the Berne Union and OECD attempt to establish and maintain discipline with respect to the use of subsidies. The Berne Union is concerned with matters related to the insurance of export credits and foreign investment. The Union presently has 36 member insurance organizations from 28 countries. Of the NICs, Hong Kong, Mexico, Singapore, and South Korea have insurance companies that are members of the Union. The OECD is responsible for establishing international guidelines on export credit terms. These guidelines, referred to as the Consensus, in effect establish an international code of conduct with respect to interest rates, repayment periods, downpayments, and credit conditions of government-supported export credits. The NICs generally follow the guidelines set by the Consensus, but they make every effort to meet foreign competition and are particularly aggressive where support for their emerging capital-intensive industries is required.* 25X1

**Table 4**
**United States: Countervailing Duties Against the Newly Industrializing Countries, 1976-82**

| Year | Country | Product | Duty *(percent)* [a] |
|---|---|---|---|
| 1976 | Brazil | Castor oil products | 11.3 |
| 1977 | Brazil | Scissors and shears | 15.6 |
| | | Cotton yarn | 19.8 |
| | South Korea | Handbags | NA |
| | Taiwan | Handbags | NA |
| 1978 | Brazil | Textiles | Waived |
| 1979 | South Korea | Bicycle tires and tubes | 0.5 |
| 1980 | Brazil | Pig iron | Case by case |
| 1981 | Mexico | Leather apparel | 5.0 |
| | Taiwan | Bicycle tires and tubes | 0.89 |
| 1982 | Mexico | Ceramic tiles | 17.36 |
| | | Toy balloons and balls | 5.97 to 6.23 |
| | | Litharge, red lead, and lead stabilizers | 3.73 |

[a] Duty is equal to the assessed value of the net subsidy.

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**Industries Promoted.** In addition to using a new mix of measures, we believe the NICs are moving away from providing support to a broad range of manufactured exports to the promotion of specific products. This is being accomplished through tax and financial incentives and, to a lesser extent, import restrictions and free trade zones. In most instances, we found that the industries promoted by these measures have at some time been targeted for expansion under the NICs' industrial development plans. 25X1

A review of NIC programs indicates that *financial incentives* are the most extensively used sector-specific measure. In Brazil, for example, over one-third of total interest rate equalization credits are extended to the transport equipment sector. The principal recipients of Mexico's credit support are the chemical, basic metal, machinery and electronic, and textile industries. Singapore's rediscounting scheme has been used to finance small- and medium-sized producers' exports of capital-intensive products. Most of South Korea's Eximbank loan commitments have supported ship exports, while Taiwan's export credits are extended principally for machinery. 25X1

**Table 5**
**Newly Industrializing Countries: Fiscal Export Incentives**

| Country | Incentives for Production of Exported Products | Main Beneficiaries | Incentives Granted to Exporting Firms | Main Beneficiaries |
|---|---|---|---|---|
| Brazil | Tax and duty breaks on imported inputs. | Transport equipment and metals. | Exemption from import duties. | All exported manufactured goods. |
| | Duty drawback. | Metallurgy, transport equipment, mechanical, and electronic machinery. | Value-added tax credits. | Transport equipment, food, metallurgy, textile, and mechanical equipment industries. |
| | | | Export-related income tax reductions. | All exported merchandise. |
| Mexico | Reduction of import duties on machinery and equipment not available domestically. | All firms that manufacture exported goods. | | |
| | Exemption from import duties on temporary imports. | All firms that manufacture exported goods. | | |
| Singapore | Tax relief for pioneer industries. | Firms that produce aircraft components and accessories, diesel and gasoline engines, compressors, transformers, electric portable tools, electrical testing and measuring equipment, microwave equipment, magnets and magnetic measuring devices, and a wide range of plastic raw materials. | Export-related income tax reductions. | Companies having export sales greater than S $100,000 and exporters of nontraditional products. |
| South Korea | Tariff rebate system. | All firms that import raw materials or components used in the production of exports. | Tax rebate on exported goods. | All exports. |
| | Tariff installment system on capital equipment imports. | Firms that manufacture goods for export. | | |
| | Special depreciation allowance. | Firms that manufacture exported goods. | | |
| Taiwan | Duty rebate on imported raw materials. | All firms that manufacture exported goods. | Export-related income tax exemption. | All exports. |
| | Duty exemption on imported machinery and equipment. | All firms that manufacture exported goods. | | |

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As a further financial incentive, the Brazilian Government provides working capital loans to export-oriented firms; Mexico offers preexport financing to aid the production of items to be exported. The working capital loans in Brazil are provided mainly for the production of fibers, fabrics, footwear, and leather products. The preexport financing scheme operated in Mexico favors the production of capital goods. 25X1

***Promotion of the Korean Shipbuilding Industry***

*The Korean shipbuilding industry is a classic example of government promotion and successful industrial development. Targeted for development in the late 1960s, the shipbuilding industry burst into the international market in the 1970s, ignored a worldwide shipbuilding recession that cut tonnage produced in half between 1976 and 1979, and eventually gained enough European, Middle Eastern, and North American customers to become the world's second-largest shipbuilder and exporter of ships. From 1971 to 1981, Korean production increased from roughly 40,000 gross tons of ships with no exports to over 1.1 billion gross tons, of which over 90 percent was exported.*

*According to industry analysts, the principal reason for the success of the industry has been price competitiveness. Estimates by the Association of Western European Shipbuilders put the Korean price advantage over European builders at 12 percent for a 1,750-TEU (20-foot-equivalent unit container) containership (roughly a $38 million price tag in Korea versus $43 million in Europe) and as high as 24 percent for a 13,600-DWT (deadweight tons) bulk carrier ($42 million versus $55 million). On average, South Korea can build ships for 15 percent less than they are built in Western Europe.* 25X1

*The price competitiveness of Korea's ships has been due to both its comparative advantage in labor costs and the government's support policies. One industry estimate puts Korean shipyard wages at one-third the level of wages in Japan. The government's long-standing support for the industry and its exports has also been an important factor. For example, all import duties and domestic taxes are waived on shipbuilding equipment and material used in shipyards. Moreover, the Korea Export-Import Bank provides concessionary export loans, which have reduced the cost of export financing by as much as 5 percentage points.* 25X1 25X1

*In 1980 and 1981, over 90 percent of the $400 million and $810 million, respectively, of export credits arranged by the Bank were for ships. These loans, in turn, financed over three-fourths of the value of the ships exported in each of these years* 25X1

The NICs generally provide some form of *tax incentives* to promote exports (table 5); those in Brazil, Singapore, and Taiwan tend to focus on specific industries. Brazil, for example, provides packages of enterprise-specific tax and duty exemptions and reductions to firms that agree to export a prearranged amount of manufactured goods. The incentives provided by Mexico and South Korea do not promote specific manufacturing sectors, but they do favor the production of manufactured goods over primary products.

The use of *import restrictions* to protect export-oriented industries varies among the NICs. Singapore and Hong Kong have virtually no controls on imports. Taiwan uses tariffs to control imports, while South Korea uses both tariffs and import licenses. Both countries have been liberalizing their import regimes, but they are still highly restrictive on imports that compete directly with export-oriented industries, which are targeted for expansion under their industrial development plans. The most restrictive import regimes are in Brazil and Mexico. Each relies on a complex system of import licenses and duties that, according to the IMF, actually discourages exports by promoting import substitution. It is in part to correct for this antiexport bias that Brazil and Mexico offer financial incentives to domestic firms to stimulate their production of exported goods. 25X1

Most of the NICs have some type of *free trade zone.* 25X1
These zones offer manufacturers of exports duty-free entry of imported materials, tax holidays, subsidized utility prices, less redtape in processing imports, and numerous other incentives. According to UN and OECD studies, these zones were an important factor in attracting the labor-intensive textile, apparel, and footwear industries that played a major role in the

early phases of the NICs' outward-looking growth strategies. The NICs' free trade zones now are crowded with factories that assemble machinery and electrical appliances and components for export.

**Outlook**

We expect that most of the NIC programs will continue to be industry-specific, but our analysis of their industrial plans and supporting trade policies indicates that the industries targeted will shift. We believe the following exports will be heavily promoted in the future:

- In Singapore, computer software and precision engineering products.
- In Taiwan, precision and heavy-duty machinery and consumer electronics.
- In South Korea, specialty vessels such as roll-on/roll-off ship and nonvessels such as offshore drilling rigs and steel structures, computers, semiconductors, and machine tools.

Because of their financial problems, we doubt that Brazil and Mexico will be able to do much about restructuring their industries for some time. As a result, their export assistance programs will probably remain focused on such industries as transport equipment, steel, and apparel. Brazil could register some gains in higher technology items, although we doubt the growth will be all that substantial.

We believe that the type of incentives offered under the NICs' export assistance programs will also change. According to statements in the NICs' industrial development plans and our discussions with US bankers and businessmen, the main constraint on the operation of the NICs' export assistance programs is the lack of financial resources. We believe that the NICs will shift away from some of the fiscal incentives and direct buyer and supplier credit programs, which require substantial government support, and instead rely more heavily on:

- Interest rate equalization programs under which an export credit agency pays the difference between the lender's cost of funds and the preferential rate charged to the exporter.
- Insurance and guarantees of export credits to protect against political and commercial risks.

By making these adjustments in their export assistance programs, we believe that the NICs can reduce their overall demand for financial capital and at the same time cover a broader range of exports. 25X1

**Implications for Trade Partners**

The NICs' advanced export assistance programs enable many NIC exporters to capitalize on the recovery in the world economy. 25X1 By having in place the trade policies that promote the export of their traditional products, the manufacturing facilities to efficiently produce a larger volume of these products, and the linkages to major retail outlets, we believe that the NICs can increase their market shares of such consumer goods as textiles, apparel, footwear, and electrical products and such industrial goods as steel and electrical machinery. This is especially likely to happen in the United States because of the NICs' strong foothold in the US market and the strength of the dollar. 25X1

We believe that in the medium term the NICs will also become accomplished exporters of selected manufactured products that they have not traditionally exported. The NICs will almost certainly not compete in the broad range of high-technology products that sell on the basis of quality and product reputation. Rather, as in the case of their clothing and footwear exports, they will locate market niches in the capital- and technology-intensive markets that can be promoted by their export incentive programs and exploited on the basis of price. As a result, many of the trade tensions and adjustment problems that exist between 25X1 the NICs and the United States, Western Europe, and Japan over labor-intensive goods will shift to new products. 25X1

Although the NICs will probably become a growing source of trade irritation to industrial countries, their economic well-being—which depends heavily on exports—is important to the West. If NICs such as Brazil and Mexico are denied access to new external markets, their export earnings potential and with it their ability to handle their financial problems will be reduced. Further financial disruptions in either of these two countries could quickly spill over to other less developed countries (LDCs). The Asian NICs, although financially better positioned, are strategically located and are important to the national security of the industrial countries. In a much less visible way, failure by the NICs could alter the perceptions other

LDCs have toward the efficacy of the capitalist versus socialist model of development. Many LDCs look to the market-oriented NICs as an example by which to model their own economies. [redacted] 25X1

Possible NIC-industrial country trade frictions could have other affects as well. The NICs have shown little interest in substantial manufactures trade with the Soviet Bloc. If Western recovery is insufficient to spark NIC export sales or the NICs perceive that they are being excluded from the gains of recovery, this could rapidly change. The NICs have already demonstrated that they will aggressively seek alternative markets, such as OPEC countries, to maintain export growth when OECD markets slump. Any decision to boost trade with the East would not only aid the Soviets economically and politically but would also complicate Western efforts to limit technology transfer to the Bloc.[4] [redacted] 25X1

Over the longer term, a loss of technology through the NICs is almost certain. The NICs' success in moving production to higher technology goods will depend on sales outlets abroad. If they are unable to achieve reasonable export volume levels, they will be unable to realize the economies of scale critical to being price competitive. This alone would spark an interest in sales to the East. At the same time the Soviets, increasingly limited in their access to Western technology, will find NIC producers an attractive alternative source of high-technology items. Competition among the NICs in their export promotion schemes will only sweeten the pot by lowering acquisition costs. As the NICs shift more toward high technology and as trade linkages with the East become established, the risk of losses will grow. [redacted] 25X1

[redacted] 25X1

Brazil

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# Appendix A

# Synopses of NIC Export Assistance Programs

## Brazil

### Overview

Since the mid-1960s, Brazilian foreign trade policy has focused on increasing the export orientation of the industrial sector. To promote exports Brasilia has established an extensive system of economic incentives, which are administered by the Foreign Trade Department of the Bank of Brazil (CACEX). Included in the system are duty rebates, export tax credits, reductions in corporate income taxes, exemptions from certain import duties, and preferential financing.

The incentives tend to focus on manufacturing subsectors. Studies prepared by the IMF, Brazilian Government, and private consultants have concluded that the export incentives weigh heavily in favor of the transport equipment, electrical equipment, textile, apparel, steel, and machinery industries. Moreover, these studies indicate the incentive system is structured to favor the development of new markets in the Middle East, Africa, and Latin America and to shift exports away from traditional US and West European markets.

Brasilia's arrangement with the IMF for extended funding has required a change in trade policy. In the course of carrying out a three-year program of economic adjustment, Brasilia has consented to a real depreciation of the cruzeiro against the dollar and approved a number of new measures to further stimulate exports. By improving the price competitiveness of exports, Brazilian authorities intend to boost the export earnings generated in the manufacturing sector—particularly high value-added exports—and to correct their mounting current account deficit. Because of its pressing foreign exchange needs, Brasilia's long-term industrial ideology has yielded to short-term pragmatism

### Supporting Policy

***Exchange Rate.*** In terms of trade policy, an important element of Brazil's economic adjustment program is the commitment to a devaluation of the cruzeiro. Following a 23-percent maxidevaluation in February 1983, the government of Brazil has been devaluing the exchange rate in line with the rate of domestic inflation to maintain rather than increase the price competitiveness of exports. 25X1

Brasilia maintains an array of exchange restrictions. These range from a progressive surtax on the remittance of profits, dividends, and royalties to a 25- 25X1
percent financial transactions tax on purchases of foreign exchange for imports of certain manufactured goods and services. According to the letter of intent, Brasilia will eliminate many of its exchange restrictions during 1983. However, embassy reporting suggests this will probably not occur immediately because of the overriding importance attached to reducing the current account deficit. 25X1

***Import Restrictions.*** Both tariff and nontariff barriers are widely used by Brazil. At present, tariffs on imported goods range up to 205 percent with the majority of goods bearing a duty between 15 and 55 percent. Brasilia also maintains a broad range of quantitative import restrictions. These include an import licensing scheme, which involves considerable 25X1
redtape, and a quota system to restrain imports of domestically produced machinery, equipment, vehicles, and spare parts. 25X1

The Brazilian Government has recently introduced a number of import restrictions to cope with its payments problems. Since late 1982 about 1,900 manufactured, semimanufactured, and primary products have been added to a list of items for which import licenses are not granted. Particularly affected are chemicals, pharmaceuticals, and machinery. Moreover, import cuts of up to 5 percent have been imposed on private firms in addition to the 10-percent cuts imposed in July 1982; state enterprises have been encouraged to further reduce their imports as well. 25X1
According to their agreement with the IMF, the

Brazilian authorities will introduce a new foreign trade system that will shift the protection of domestic industry away from quantitative restrictions to tariffs and thereby improve the predictability of import regulation. [redacted]

According to several studies, Brazil's system of import restrictions actually discouraged exports by shifting resources into import substitution industries. Although authorities were attempting to change this antiexport bias before the recent financial crisis, we believe any gains they achieved will be more than offset as new import restrictions encourage firms to produce goods that can replace imports. [redacted]

***Fiscal Incentives.*** The most significant and perhaps best known of Brazil's export incentives are its tax exemptions and credits. All exports of manufactured goods are exempt from two value-added taxes—the IPI (Imposto Sobre Produtos Industrializados), which is a federal tax of up to 31 percent levied on merchandise produced, and the ICM (Imposto de Circulacao de Mercadorias), which is an 11-percent state tax on merchandise. [redacted]

The Brazilian Government also grants an IPI tax credit to firms that export certain manufactured goods. Called a *credito premio,* this rebate to exporters can be applied toward either the payment of IPI taxes on any other operation of the firm or, if necessary, can be shifted to subsidiaries or to suppliers of inputs. The IMF estimates that the value of the IPI rebate was $2.2 billion in 1982, equivalent to about 13 percent of the value of manufactured goods exported in 1981. Accounting for roughly 60 percent of the total fiscal incentives offered to exporters, the rebate goes chiefly to the transport equipment, food, metallurgy, textiles, and mechanical equipment industries. [redacted]

The rebates have long irritated US and other competitors of Brazilian goods who consider them to be unfair export subsidies. In response to pressure from these parties, Brasilia phased out the rebate in 1979. However, it was reinstated in April 1981 with the understanding that it would be eliminated in 1983. In its recent letter of intent to the IMF, Brasilia announced that the rebate would be extended through April 1985 at its level of 11 percent. [redacted]

Brazilian firms also benefit from an export-related income tax exemption. All firms that export may reduce their taxable income by the percent of total sales represented by exported merchandise or services. Moreover, income tax deductions are allowed for export promotion expenses incurred abroad and for the costs connected with the firm's overseas sales operations. According to the IMF, these tax provisions provide only a modest incentive and are to be abolished at the end of 1985. [redacted]

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Another type of fiscal incentive for exports—credits for the production of export products—is provided chiefly through BEFIEX (Beneficios Fiscais e Programas Especiais de Exportacao), a system of enterprise-specific export incentives provided in exchange for a commitment from each participating firm to reach agreed export targets, generally over a period of 10 years. The typical incentive package contains a 70- to 90-percent duty and tax reduction on imports of machinery and equipment and a 50-percent reduction of duties and taxes on raw materials. The key advantages of the BEFIEX system are that the imports received may be used for domestic as well as export production. According to IMF data, the program, which was established in 1972, covers 23 percent of all manufactures exports, an increase of 7 percentage points since 1977. The principal recipient of BEFIEX incentives is the transport equipment sector, which accounts for over three-fourths of the total benefits conveyed under the program. [redacted]

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An additional way for firms to reduce the cost of inputs for export is the duty drawback system. Under this scheme, enterprises are exempt from the payment of import duties and certain taxes on inputs used in the production of manufactured exports. According to diplomatic reporting, $600 million of duties and taxes were suspended under this program in 1981. The main beneficiaries were the metallurgy, mechanical and electronic machinery, and transport equipment industries. Together, they accounted for over 70 percent of the total exemptions. [redacted]

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According to diplomatic reporting, a new export incentive called the Green-Yellow drawback went into effect on 28 March 1983. Under this scheme, a tax

25X1

exemption for IPI and ICM taxes is granted to domestic manufacturers of inputs that are incorporated into products that are subsequently exported. Currently, the textile industry is the only beneficiary of the Green-Yellow drawback. However, embassy reporting indicates that the government of Brazil is considering extending it to the nonferrous metal, autoparts, or alcohol sectors. [redacted]

***Financial Incentives.*** Two basic types of official export financing are offered in Brazil—an interest rate equalization program and a direct working capital loan program. Under the interest rate equalization program, Brazilian exporters arrange with approved Brazilian commercial banks for buyer and supplier credits at concessionary terms. CACEX then covers the difference between the concessionary rate charged to the exporter and the lending institution's actual cost of obtaining these funds. Depending on the goods exported and the length of the repayment period, CACEX will finance up to 85 percent of the export at interest rates ranging from 7.5 to 10 percent. [redacted]

The IMF indicates that the credits extended by CACEX increased from $700 million in 1976 to a peak of $1.7 billion in 1980. Although CACEX has continued to expand the value of credits extended, the depreciation of the cruzeiro reduced their dollar value to only $800 million in 1982. Estimates from CACEX officials indicate that over one-third of these credits are extended to the transportation equipment sector. Other major recipients include the construction, energy, and communications equipment industries. [redacted]

In addition, working capital loans are provided to firms that produce manufactured exports. Governed by Central Bank Resolution 674, the program offers highly subsidized, short-term cruzeiro loans through commercial, investment, and state development banks, using the discount window of the Central Bank. The amount of subsidized working capital that each firm is eligible to receive is determined by CACEX in accordance with an involved set of regulations. CACEX issues firms a certificate, which subsequently allows them to obtain Resolution 674 resources through the commercial banks. This certificate is awarded on the basis of the products manufactured and the value of the firm's net exports in the previous year [redacted]

[redacted] 25X1
IMF indicate that the average subsidy rate under Resolution 674 was at most 8 percent in 1981. The products most favored by the subsidy are fibers, fabrics, apparel, footwear, and leather products, with a subsidy close to or above 11 percent of the export value. [redacted] 25X1 25X1 25X1

As part of its economic adjustment program with the IMF, Brasilia is attempting to reduce its massive export credit subsidy programs. According to diplomatic reporting, the Monetary Budget for 1983 allows a 15-percent increase in the volume of subsidized export credit. This is intended to be in line with the projected growth of industrial exports for the year. The subsidy element of these programs, however, is to be reduced. This reflects both a lower projected rate of inflation and a shift in composition of credit programs away from the more heavily subsidized Central Bank working capital loan programs to the less subsidized Bank of Brazil interest rate equalization programs. [redacted] 25X1 25X1

The government of Brazil has recently introduced PROEX, a financial program used to stimulate exports. Companies that achieve agreed-upon export targets can receive funding equivalent to 30 percent of the realized increase in the company's export earnings over a two-year period. The company can then spend up to 70 percent of the PROEX funds for equipment and 30 percent for working capital. As with most incentive programs, only manufacturing firms with at least 51-percent Brazilian ownership are eligible for PROEX funding. [redacted] 25X1 25X1

***Government Promotion.*** The government also sponsors trade fairs and other promotions to spur exports. The primary responsibility for these is divided between CACEX and the Ministry of Foreign Relations (Itamarati), with CACEX responsible for promotions within Brazil and Itamarati responsible for those abroad. In practice, however, considerable overlap exists between the two agencies. [redacted] 25X1

***Other.*** The Instituto de Ressguros do Brazil (IRB), a government-controlled agency, provides three types of export insurance to Brazilian exporters. The coverage includes political and extraordinary risk, commercial 25X1

**Table A-1**
**Brazil: Importance of Trading Companies**

| Year | Total Brazilian Exports *(billion US $)* | Exports by Trading Companies *(billion US $)* | Share of Total Exports *(percent)* |
|---|---|---|---|
| 1976 | 10.1 | 0.9 | 8.9 |
| 1977 | 12.1 | 1.5 | 12.4 |
| 1978 | 12.7 | 1.7 | 13.4 |
| 1979 | 15.2 | 2.4 | 15.8 |
| 1980 | 20.1 | 3.7 | 18.4 |
| 1981 | 23.2 | 4.5 | 19.4 |
| 1982 | 19.9 | 5.5 | 27.7 |

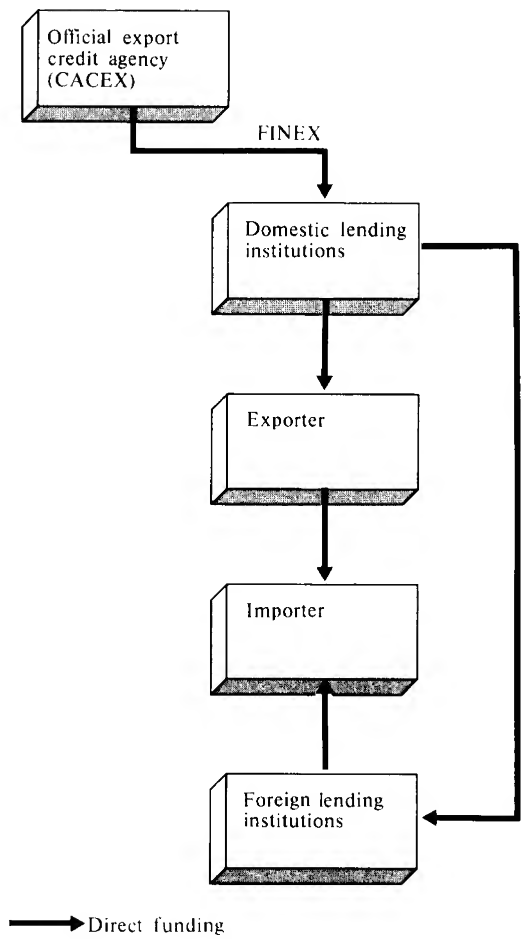
[redacted]

risk (primarily for commodity exporters), and breach-of-contract risk (for manufacturers). Premiums vary according to the risks and repayment terms. For political and extraordinary risk coverage, the premiums range from 0.18 percent for a six-month transaction to 2.49 percent for five years. By comparison, the premiums for commercial risk coverage range from 0.48 percent for six months to 3.33 percent for five years. [redacted]

To support companies that are not large or sophisticated enough to engage in export trade, Brasilia promotes the creation and operation of trading companies. Because these companies are provided subsidized credits, are exempt from the value-added and excise taxes on exported products and the income tax on export profits, and are eligible for the IPI rebate, they have become an important factor in Brazil's trade sector. In 1982 the trading companies registered a 22-percent increase in exports over 1981 and increased their share of total exports to 28 percent, up from 19 percent in 1981 (table A-1). Trading company officials predict that the trading companies will account for $7 billion or one-third of the total exports targeted for 1983. [redacted]

In conjunction with the overall export incentive program, the government of Brazil maintains six free trade zones—Manaus, Belem, Corumba, Parangua, Porto Velho, and Santos. According to government promotion brochures, the most ambitious plans have

**Figure A-1**
**Brazil: Flow of Export Financing**

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[redacted]
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been devised for Manaus, which is in the heart of the Amazon jungle. Manaus administrators say they want to attract the entertainment electronics industry away from Sao Paulo and to become a self-sufficient industrial center. [redacted]

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Hong Kong

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## Hong Kong

### Overview

The Hong Kong Government maintains a laissez faire stance toward trade and enterprise. There are few regulations, no export subsidies, and, as a free port, no general tariff. The government's Trade Industry and Customs Department has primary responsibility for overseas commercial relations, trade controls, and collecting revenue from dutiable commodities. [redacted] 25X1

One major problem plagues Hong Kong—the future of the colony when Britain's lease with China expires in 1997. We believe that, over the next five to seven years, the continued political uncertainty surrounding the 1997 issue will restrain economic growth and deepen economic downturns, making it more difficult for the government of Hong Kong to pursue its traditional noninterventionist trade and industrial policies. [redacted] 25X1

### Supporting Policy

***Exchange Rate.*** There are no exchange controls. [redacted] 25X1

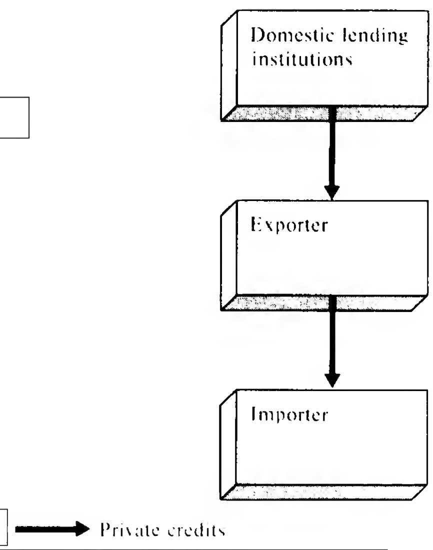
***Import Restrictions.*** Other than controls on 20 items for reasons of health, safety, and security, imports are free from licensing control. [redacted]

***Fiscal Incentives.*** Hong Kong has no protective tariffs, capital gains taxes, or corporate income tax. Gross business profits are taxed at a flat rate of 17 percent, the lowest tax rate in Asia. Offshore profits are not taxed. [redacted]

***Financial Incentives.*** There are no subsidized export programs in Hong Kong. [redacted]

***Government Promotion.*** The Hong Kong Trade Development Council has primary responsibility for promoting and developing Hong Kong's exports. The council participates in many international trade fairs and publishes four periodicals to keep overseas businessmen informed of the latest financial and industrial developments in Hong Kong. It also organizes business group visits to explore new markets and strengthen existing trade ties and has opened industrial promotion offices in San Francisco, Tokyo, London, and Stuttgart. [redacted] 25X1

**Figure A-2**
**Hong Kong: Flow of Export Financing**




[redacted] 25X1
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***Other.*** The Hong Kong Export Credit Insurance Corporation (HKECIC), a government entity, facilitates trade by protecting exporters against nonpayment for goods and services sold abroad on credit. It also provides export finance guarantees to lending institutions. HKECIC is a member of the International Union of Credit and Investment Insurance (the Berne Union). [redacted] 25X1

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Mexico

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## Mexico

### Overview

In 1979 the Mexican Government introduced an Industrial Development Plan for the 1980s that included provisions for concentrating export incentives on industries in which Mexico had the potential to become competitive in world markets. Support was to be provided for industries:

- With established world markets where the limiting factor was supply rather than demand (such as mining).
- That increased the value of local raw materials (such as secondary petrochemicals, chemicals, and metal products).
- That had suffered declining output from the lack of investment (such as textiles and other traditional export industries).
- Requiring large-scale production to supply domestic and foreign demand (such as steel and capital goods).
- Responsible for considerable trade deficits because of foreign control and limited access to world markets (such as the automobile and rubber industries).

[redacted]

To promote the development and export potential of these industries, the Mexican Government relied on a complex system of import tariffs and licenses coupled with several different types of fiscal and financial incentives for exports. However, according to the IMF, these mechanisms have frequently been applied haphazardly, resulting in wide disparities in the incentives and protection granted to different industries. In general, the policies benefited final products in the industrial sector and, to a lesser extent, agriculture, while they discriminated against the intermediate-good industries, mining, and traditional exports originally targeted for development under the Industrial Development Plan. [redacted]

Another major Mexican policy, laid out in the Industrial Development Plan, is to diversify trading partners and reduce the overwhelming involvement with the United States. At present, it emphasizes building trade relationships with other less developed countries. [redacted]

Serious financial problems in late 1982 and 1983 forced the government of Mexico to diverge from its Industrial Development Plan. To remedy the financial crisis, the government recently introduced a new foreign trade policy. In its letter of understanding with the IMF, the government agreed to changes in the tariff structure, export incentives, import permit requirements, and the exchange rate system. These revisions are intended to reduce subsidies to industries benefiting from inordinate promotion and enhance the competitive position of Mexico's other export industries [redacted] 25X1

### Supporting Policy

***Exchange Rate.*** At IMF direction, Mexican authorities liberalized the exchange rate system and eliminated restrictions on many types of foreign exchange payments. The exchange rate system has two basic rates—a controlled rate for a specified list of transactions and a "free rate" for all others—and a foreign exchange restriction on the repayment of foreign debt obligations. [redacted] 25X1

***Import Restrictions.*** Mexico has traditionally operated a fairly restrictive regime of import licenses and 25X1 duties. In 1981 import licenses were required for 27 percent of the items listed in Mexico's General Import Tariff, accounting for almost 80 percent of the total value of imports. Licenses can be denied if: the import is a luxury good, the import price is higher than a reference international price set by the government, a domestic product of similar quality is available, import quotas have been exceeded, or the import would necessitate too many future imports. According to the IMF, the *ad valorem* duty rates range up to 100 percent, the rate being progressively higher for luxury goods and for goods that are produced domestically. Tariffs on raw materials are often zero, about 20 percent for capital equipment for development, 20 to 60 percent for less needed equipment, and 60 to 100 25X1 percent for luxury and consumer goods. [redacted] 25X1

In mid-May, Mexico City announced changes in the treatment of both imports and exports. According to embassy reporting, export permits will no longer be

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required on 94 percent of exports, and the import duty on nearly 8,000 import items—mostly raw materials and spare parts—was either reduced or eliminated. Moreover, most export regulations and incentive programs will now be administered by the expanded Mexican Foreign Trade Institute (IMCE) rather than the five or more agencies with which exporters previously had to contend. [redacted]

*Fiscal Incentives.* The government of Mexico grants several types of fiscal incentives to domestic producers and exporters. In our judgment, the most important change in the structure of Mexico's tax incentives for exports has been the suspension of the Certificados de Devolucion de Impestos (CEDI). The CEDI was a tax certificate issued by the government in an amount equal to a percentage of the value of a firm's exports. This certificate was then used by the firm as a credit against a wide range of federal tax liabilities. Until its suspension in August 1982, the CEDI program was the most important fiscal incentive provided to exports, reducing the price of exports by as much as 10 to 15 percent. The principal recipients of these tax credits were manufactured and semimanufactured products. As Mexico City has only agreed to suspend rather than eliminate the CEDI, it could be reinstated. [redacted]

Three fiscal incentive programs are in operation. Under the first, a rebate of up to 100 percent of the value of import duties is granted on machinery and equipment used in the production of exports. To qualify, the firm must demonstrate that the machinery is not produced in Mexico in sufficient quantity and that the new machinery will increase the overall productive capacity of the firm. The amount of rebate provided depends on both the increase in export volume generated by the equipment and the geographic location of the plant. Under the second program, the import tariff law provides for temporary duty-free import materials, components, and supplies not available in Mexico for production of goods that will be exported. [redacted]

Certificates of Fiscal Promotion (CEPROFIs), the third fiscal incentive program, operates much like the CEDI program. However, rather than providing tax credits for the value of goods exported, CEPROFI tax certificates are granted to firms that carry out investments in high-priority industrial activities. The amount of the CEPROFI is based on the location of the activity, the number of jobs generated, and the value of the investment in new plants and equipment. Although the CEPROFI subsidies are for domestic production, they indirectly stimulate Mexican exports. [redacted] 25X1

*Financial Incentives.* The principal source of export financing in Mexico is the Fund for the Promotion of Mexican Products (FOMEX). A trust fund administered by the Bank of Mexico, FOMEX operates as a discounting facility to Mexican banks for the promotion of manufactured goods exports and for the development of import substitution industries producing capital and consumer goods. According to FOMEX publications, roughly two-thirds of the $3.1 billion of authorized financing in 1981 was directed toward the promotion of manufactured goods exports. [redacted] 25X1

The FOMEX export-related programs provide both export and preexport financing. In 1981 export financing accounted for one-half of FOMEX's total funding. This support is provided primarily for supplier credit transactions, but limited buyer credit support 25X1 is available under basically the same program. Depending on the type of goods exported, credit terms vary from 30 days to 10 years, with capital goods obtaining the longer terms. The percentage of the contract financed by FOMEX varies with the repayment period and Mexican content of the transaction. The minimum Mexican content requirement is 30 percent. In 1981 the interest rate charged for export financing ranged from 6 to 8.75 percent (table A-2). According to FOMEX's annual report, chemicals and related products, machinery and basic metals, electronic materials, and textiles are the principal recipients of FOMEX credit support. [redacted] 25X1

Preexport financing accounts for almost one-fifth of total FOMEX financing and is available for a wide 25X1 range of functions. These include financing for the domestic production of an item that is subsequently



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**Table A-2**
**Mexico: FOMEX Export Financing Rates, 1981**

*Percent*

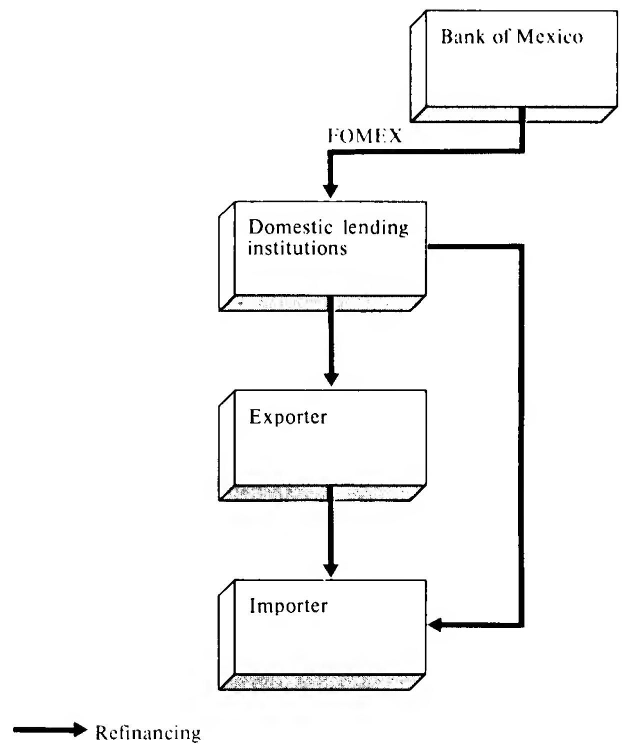
| Country Type | Less Than Two Years | Two to Five Years | Five to 8.5 Years | 8.5 to 10 Years |
|---|---|---|---|---|
| Relatively rich | 6 | 8.5 | 8.75 | |
| Intermediate | 6 | 8.0 | 8.50 | |
| Relatively poor | 6 | 7.5 | 7.75 | 7.75 |

exported as well as for imports used in the production of exports. For products with Mexican content of between 30 to 50 percent, financing can be obtained for 100 percent of the Mexican content. If Mexican content exceeds 50 percent, 100 percent of the material cost or 70 to 85 percent of the f.o.b. price may be financed. In mid-1982 the maximum interest rate that credit institutions charged borrowers for FOMEX preexport financing was 8 percent. FOMEX preexport financing has been provided primarily for capital goods exports.

As part of the package of foreign trade reforms announced in May, the Mexican Government will reduce redtape and provide short-term financial support for export-related activities. The financial efforts to assist firms in developing exports include a 400 billion peso ($2.7 billion) credit program that will be administered by Bancomex, the government foreign trade bank. A credit program now being negotiated with the World Bank will provide funds to exporters at preferred rates through several existing government trust funds, and government export guarantees will be raised from 109 million pesos ($2.0 million) in 1982 to 12.5 billion pesos ($84 million) this year

***Government Promotion.*** IMCE is the principal government entity charged with promoting exports. IMCE has representatives in the capitals of most of Mexico's major trading partners and many cities in the United States. It provides such services as commercial information, marketing research, statistical data, and training to Mexican executives. According to embassy reports, IMCE has had a history of

**Figure A-3**
**Mexico: Flow of Export Financing**

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frequent personnel changes and bureaucratic problems, which have prevented it from having much of an impact on Mexico's export performance. 25X1

25X1

***Other.*** Commercial risk insurance for export transactions is provided by the government's Compania Mexicana de Seguros de Credito (COMESEC). The premium ranges and averages are not published by COMESEC. FOMEX provides both political risk insurance and credit guarantees. FOMEX guarantees

will cover up to 90 percent of an export loan. Premiums range from 1.25 to 4.6 percent, depending on the country, credit terms, and nature of the transaction. [redacted] 25X1

The states of Baja California, the city of Agua Paieta, and a triangular area in the state of Sonora, as well as a number of ports in the southern part of Mexico have been established as free trade zones. Manufacturers in the zones operate with a minimum of government control. [redacted] 25X1



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Singapore

## Singapore

### Overview

In the past Singapore generally eschewed direct export incentives because most manufactured products were already highly competitive in international markets and were in growing demand. The government, however, has recently begun to modify this policy because of rising international protectionism and a decline in the competitiveness of traditional exports. To expand into higher value-added exports, the government has introduced a package of incentives designed to restructure the industrial sector away from the production of labor-intensive products toward capital-, skill-, and technology-intensive industries. As part of this package, the government has introduced tax breaks for the export promotion expenses incurred by firms and concessional export financing to promote capital-intensive industries. [redacted]

### Supporting Policy

***Exchange Rate.*** Since 1978 all controls on foreign exchange transactions have been removed. [redacted] 25X1

***Import Restrictions.*** All imports enter freely except a few that are controlled for health and security reasons. [redacted]

***Fiscal Incentives.*** Singapore offers several fiscal incentives to promote exports. The major incentives include:

- Tax relief for pioneer industries. To encourage the establishment of specific export-oriented industries, the Minister for Finance has published a list of higher technology industries eligible for "pioneer status." On the list are aircraft components and accessories, compressors, transformers, diesel and gasoline engines, electrical testing and measuring instruments, electric portable tools, telephone exchange equipment, microwave equipment, magnets and magnetic materials, and a range of plastic raw materials such as polyethylene, polystyrene, polyvinylidene chloride, and other resins. Additional products may be added to the list as the Minister for Finance considers warranted. Pioneer status exempts these industries from the 40-percent corporate income tax for five to 10 years from the date they commence commercial production. According to the statutes, the length of the tax exemption granted depends upon, among other criteria, the merits of the project, such as type of product manufactured, investment level, and transfer of skills and technology.

- Tax relief on export profits. Companies having export sales of not less than $50,000 and totaling at least 20 percent of total sales are eligible for a 90-percent reduction in the corporate tax rate (from 40 to 4 percent) on profits arising from exports. If the company has not been granted pioneer status, it is eligible for five years of tax relief. A pioneer enterprise is eligible for three years after the expiration of its pioneer status. If the enterprise incurs a fixed capital expenditure of not more than $500 million or not less than $75 million and provided 50 percent of the company's paid-up capital is held by permanent residents of Singapore, then its tax relief 25X1 may be extended to 15 years if it is not a pioneer enterprise or for 10 years after the expiration of its pioneer status.

- Tax relief for exporters. Companies that export more than $5 million per year of qualifying Singapore manufactured goods or traditional commodities, or $10 million per year of nontraditional 25X1 commodities (excluding tin, natural rubber, palm oil, coconut oil, logs, sawn timber, petroleum, and spices) are entitled to a 20-percent corporate tax rate for a period of five years.

- Double deduction for export promotion expenses. Singapore manufacturers, exporters, banks, and traders participating in an approved overseas trade office to promote the export of Singapore manufactured goods may claim a double deduction for the promotional expenses incurred in the first two years of operation. [redacted] 25X1

***Financial Incentives.*** Two major forms of export financing are offered in Singapore, through the Fixed Rate Export Finance program (FREF). Under FREF's buyer credit program, a lending institution in Singapore lends directly to an overseas buyer or bank

**Table A-3**
**Singapore: ECICS Fixed Rate Export Finance Scheme Rates**

*Percent*

| Country Classification [a] | FREF Contract Credit Period | | | OECD Consensus Contract Credit Period | | |
|---|---|---|---|---|---|---|
| | Two to Five Years | Five to 10 Years | Over 10 Years | Two to Five Years | Five to 10 Years | Over 10 Years |
| **Singapore dollars** | | | | | | |
| Rich | 11.00 | 11.25 | 11.25 | | | |
| Intermediate | 10.50 | 11.00 | 11.00 | | | |
| Poor | 10.13 | 10.25 | 10.25 | | | |
| **US dollars** | | | | | | |
| Rich | 11.63 | 11.63 | 11.63 | 11.00 | 11.25 | NA |
| Intermediate | 11.38 | 11.38 | 11.38 | 10.50 | 11.00 | NA |
| Poor | 11.25 | 11.25 | 11.25 | 10.00 | 10.00 | 10.00 |

[a] These classifications are based on World Bank per capita GNP data for 1974. Rich is greater than $3,000, intermediate is between $1,000 and $3,000, and poor is less than $1,000.

[redacted] 25X1

on behalf of the buyer. In the supplier credit program, the lending institution in Singapore offers financing directly to an exporter. In both cases the lender can then apply for the Export Credit Insurance Corporation of Singapore Ltd.'s (ECICS) interest rate equalization. ECICS will cover the difference between the lender's cost of funding the export credit and a fixed rate set by the Ministry of Finance. The fixed rate is revised quarterly. [redacted]

FREF funding is provided for medium- and long-term transactions (two to 10 years) and there is no minimum Singapore-content requirement. FREF support may be used for up to 80 percent of the Singapore content of oil rigs and 85 percent of the Singapore content of other capital goods. According to FREF data, the interest rates offered for export credits depend on the country classification, currency of the contract, and credit period. The interest rate structure used from 1 April through 30 June 1982 is given in table A-3. For comparison, the OECD Consensus or Guidelines for Officially Supported Export Credits for that period is also provided. Because of recent funding cutbacks, the FREF program has been temporarily suspended. [redacted]

Since 1975 the Monetary Authority of Singapore (MAS) has provided export credit support through a rediscount window for commercial banks. After agreeing to finance an exporter, the commercial bank can rediscount the full value of the export credit with the MAS at a concessional rate. The loan is for three months but may be extended another three months. The discount rate set by the MAS is generally 1.5 percentage points below the Singapore prime rate. Banks, according to MAS publications, are allowed to charge a commission of no more than 1.5 percent of the export credit. Small-scale exporters, therefore, are able to receive export funding at least at the prime rate. Table A-4 shows that the proportion of exports financed under this scheme has dropped in recent years. In 1981 petroleum and nonfuel primary products were excluded from coverage in line with the government's policy of weeding out labor-intensive industries. At present, the scheme is designed to provide small- and medium-sized exporters a convenient facility to finance their capital-intensive exports. [redacted]

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**Table A-4**
**Singapore: Exports Financed Under the MAS Rediscounting Scheme**

| Year | Gross Amount Rediscounted *(million US $)* | Total Exports *(million US $)* | Share of Exports Financed *(percent)* |
|---|---|---|---|
| 1975 | 36 | 5,381 | 0.7 |
| 1976 | 195 | 6,583 | 3.0 |
| 1977 | 458 | 8,237 | 5.6 |
| 1978 | 740 | 10,108 | 7.3 |
| 1979 | 1,193 | 14,225 | 8.4 |
| 1980 | 1,480 | 19,361 | 7.6 |
| 1981 | 1,295 | 20,961 | 6.2 |

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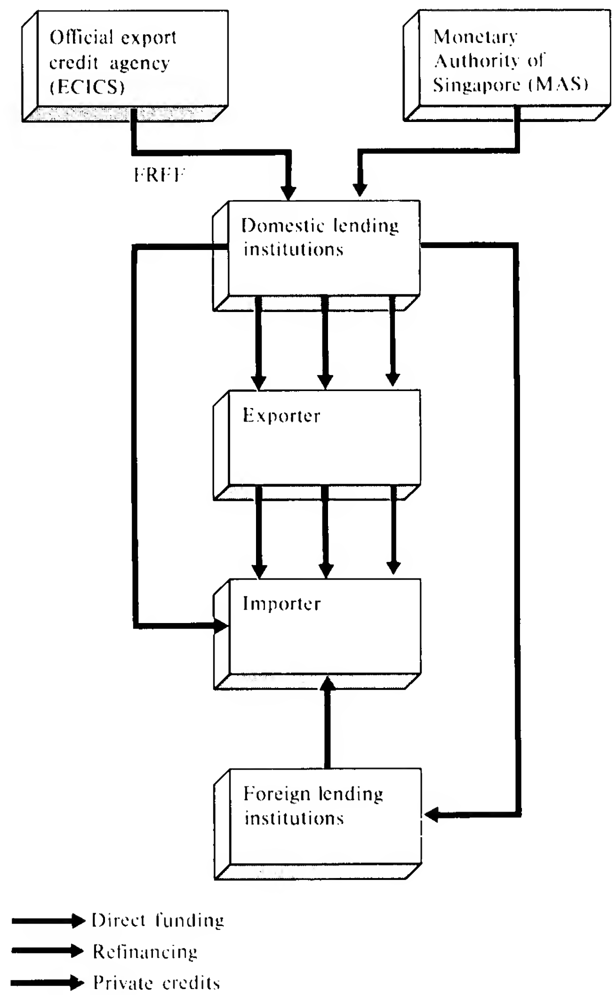
In a special program the Ministry of Finance provides financial assistance for buyer and supplier credits related to the construction of ships in Singapore. The Ministry finances up to 85 percent of the contract for a Singapore-registered shipping company and 80 percent of the contract for a non-Singapore-registered shipping company. For the former, up to one year is allowed for drawdown, followed by two years grace, and eight years repayment. Ships not owned by a Singapore shipping company are not allowed a grace period but have eight and one half years to repay. As of April 1982, the interest rates were fixed at 10 percent for Singapore dollars and 12 percent for US dollars. 25X1

Although the government of Singapore has publicly stated that it prefers each local firm to promote its own exports, it conducts trade fairs in several overseas markets. The Trade and Development Board has announced plans to conduct 36 trade fairs in traditional markets in 1983, up from 24 in 1982. It also plans to send several survey missions to new markets in Africa, Latin America, and the Pacific islands. 25X1

***Other.*** The Export Credit Insurance Corporation of Singapore Ltd. also provides insurance coverage to Singapore exporters against nonpayment caused by political and economic upheavals in the buyer's country. ECICS also offers guarantees to bankers covering short-, medium-, and long-term credit needs of local exporters. ECICS has been a full member of the Berne Union since June 1979. 25X1

**Figure A-4**
**Singapore: Flow of Export Financing**

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South Korea

## South Korea

### Overview

In 1982 Seoul introduced a Five-Year Economic and Social Development Plan, which espouses less intervention in economic management than earlier plans. For the export sector, the objectives outlined in the Plan changed from achieving specific import and export targets to strengthening overall Korean export competitiveness. According to the IMF, to achieve the growth and diversification of exports envisioned in the Plan, Seoul intends to liberalize imports, restructure tariffs, gradually eliminate short-term preferential export credits, and expand long-term buyer credits for capital goods. [redacted]

Gloomy projections for trade with the recession-hit West forced Seoul to look elsewhere for new markets. Press reports indicate that leading manufacturers are exploring several African markets—in particular Kenya, Gabon, Senegal, and Nigeria—as potential trade partners. Moreover, [redacted] expansion of direct and indirect trade with China, the USSR, Czechoslovakia, Yugoslavia, Romania, and Vietnam. However, because of political differences—which limit economic exchange to small amounts of indirect trade—we do not expect South Korea to become an important supplier to the Soviet Bloc in the near future. [redacted]

### Supporting Policy

***Exchange Rate.*** Korea operates a flexible exchange rate regime whereby the Korean won is linked to a multicurrency basket. At present, there are no foreign exchange regulations that significantly affect the flow of trade. [redacted]

***Import Restrictions.*** All imports into Korea require an import license. Applications are either automatically approved, subject to limits set by the Foreign Exchange Supply and Demand Plan, or approved case by case for restricted commodities. According to embassy reports, the list of restricted commodities is revised yearly under the Annual Trade Plan and is one of the basic measures used by Seoul to protect domestic manufacturers from import competition. Included in this list are such goods as shoes, apparel, computers, and machine tools. [redacted]

In May 1978 Seoul initiated a major import liberalization program. Its objectives, according to the IMF, are to improve the structure of industry by removing price distortions and enhancing competition, to stabilize domestic prices by increasing supplies, and to facilitate trade negotiations with countries restricting imports from Korea. [redacted] 25X1

Considerable progress has been made in liberalizing the import regime. Embassy reports indicate that between 1977 and 1982 the share of imports on the automatic approval list rose from 53 percent to 77 percent of all commodity categories in Customs Cooperation Council Nomenclature (CCCN).[5] As of 1 July this ratio was increased to 80 percent. Seoul 25X1 aims to increase the number of import categories on the automatic approval list to 90 percent by 1986. The majority of the liberalized goods have been raw materials and capital goods, but increasingly consumer nondurables and newly competitive exportables are being included. Based on the automatic import category listing, it appears that the import regime is still 25X1 heavily protective of goods that either compete direct- 25X1 ly with industries that Seoul has targeted for further expansion or that add to a severe Korean trade imbalance with selected countries, specifically Japan. [redacted] 25X1

***Financial Incentives.*** According to IMF and embassy reports, Seoul offers several tariff incentives and tax 25X1 benefits to exporters. Under its system of flexible tariffs, Seoul can raise or lower the tariffs on selected imports to attain certain short-term economic goals. The most recent revisions were announced publicly in June 1982. Tariffs on 14 raw materials used by export processing industries were dropped by 10 to 20 percentage points to improve export competitiveness, and 25X1 the duties on 26 intermediate products were reduced to assist the electronics, textile, and machinery industries. These revisions, although not significantly reducing overall tariff barriers, are in line with previous Korean moves toward the gradual liberalization of imports. [redacted] 25X1

[5] Data are not readily available to compute the share of the total value of Korean imports automatically approved. Because of the capital and technology intensity of restricted imports, we believe that this ratio is considerably smaller than the 80 percent calculated for the commodity categories. [redacted] 25X1

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The tariff system, according to the IMF, also offers a rebate mechanism and installment plan to exporters:

- Under the tariff rebate system, Korean firms that import raw materials or components used in the production of exported goods receive a rebate on the tariffs paid for these imports. In theory, these tariffs are to be paid when the commodities are imported and rebated after the final product is exported. In practice, however, the importer takes out a promissory note of two to four months' duration that is canceled if the exports are made within the specified period.

- Under the tariff installment system, all tariffs levied on capital equipment imports, which are specified by the Ministry of Finance and used for manufacturing exported goods, may be paid by industries over a two- to five-year period. [redacted]

Korean exporters are also entitled to several tax benefits:

- A rebate of the 10-percent value-added tax is available on goods destined for export or on earnings from overseas services.

- Special depreciation allowances of up to 30 percent are allowed for firms that manufacture exported goods.

- Costs related to the exploitation of overseas markets may be treated as an expense for tax purposes. Overseas construction firms receive a five-year taxable income reduction equivalent to 2 percent of foreign exchange earnings and a 30-percent special depreciation on all machinery purchases. [redacted]

***Financial Incentives.*** The Korean Government has established a broad range of short-, medium-, and long-term financial instruments, which offer preferential terms to Korean exporters. Short-term export financing is extended by commercial banks. These loans generally do not exceed 90 days and are based upon the value of the firm's total net foreign exchange earnings in the previous year. They are available for the procurement of raw materials and finished goods used in the production of exports; for overseas construction and supply of services; and for financing the collection and stockpiling of designated agricultural and marine product exports. [redacted]

**Table A-5**
**South Korea: Subsidized Export Loans From Commercial Money Banks**

| Year | Export Loans Outstanding *(billion US $)* | Share of Subsidized Credits to Manufacturing Sector *(percent)* |
|---|---|---|
| 1977 | 1.2 | 56 |
| 1978 | 1.8 | 62 |
| 1979 | 2.5 | 67 |
| 1980 | 2.8 | 72 |
| 1981 | 3.2 | 72 |

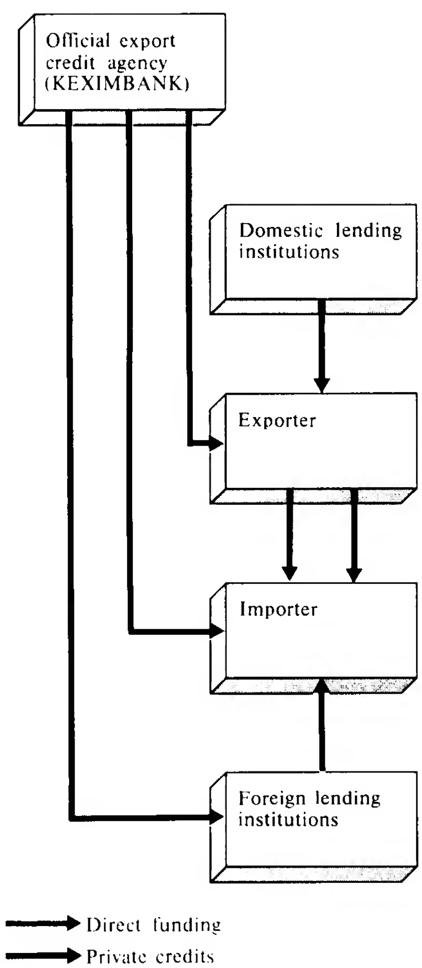
[redacted] 25X1

These loans have been an important element of Korea's support for export industries. IMF data indicate that at the beginning of 1981 these loans covered 88 percent of the total value of goods exported. They have also accounted for almost three-fourths of all preferential bank lending to the manufacturing sector (table A-5). The importance of these preferential loans is also underscored by the fact that export-related refinancing has amounted to about 30 percent of the total claims by banks on the Bank of Korea. [redacted]

According to embassy reports, Seoul has gradually reduced the differential between the prime and preferential interest rates and will phase out short-term preferential export credits by 1986. In 1981 the interest rate applied on short-term export loans was 12 percent compared with the average prime lending rate of 16.5 percent. By mid-1982, the preferential rate and the prime rate were lowered to 10 percent.

[redacted]

**Figure A-5**
**South Korea: Flow of Export Financing**




[redacted]
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Although Seoul has eliminated the interest subsidy on short-term export loans, funding can be replaced with medium- and long-term export credits. The principal source of subsidized medium- and long-term export financing is the Export-Import Bank of Korea (Eximbank). Established in 1976 the Eximbank offers buyer credits, supplier credits, and several special credit programs. Although authorized to provide refinancing and discounting, the Eximbank does not offer either type of funding. [redacted] 25X1

According to Eximbank data, the bulk of its resources, over 90 percent in 1980, go to funding supplier credits. This program has historically received the greatest emphasis because it provides the most direct means of extending financial support for export transactions. The supplier credit program is designed to encourage the export of capital goods and services that normally involve larger credits and longer repayment terms than the average Korean manufacturer or commercial bank is prepared to provide. Currently, Eximbank applies a fixed 9-percent interest charge on these loans. [redacted] 25X1

The buyer credit program allows either the buyer or financial institution in the foreign country access to Eximbank preferential financing. Called a Direct Loan, these credits are for three to 10 years, cover up to 70 percent of the contract amount, and carry an interest rate that generally ranges between 9.5 and 10 percent. In 1980 this program accounted for less than 5 percent of Eximbank funding. [redacted] 25X1

The remainder of Eximbank funding is provided for the development and acquisition of overseas resources. According to embassy reports, the main objective of these programs is to ensure access to resources that will be needed to manufacture exported products. [redacted] 25X1

To achieve the growth and diversification of exports envisioned under the Fifth Five-Year Plan, the IMF and embassy report that Seoul will expand the financing programs offered by the Eximbank. In 1981 the bank's loans covered just over 4 percent of total exports; by 1986 Korean planners see the bank lending some $4 billion covering over 7 percent of projected exports. The apportioning of these loans will also be changed. In the 1971-80 period, the most important use of these loans was to support ship exports (65 percent) and exports of industrial plants 25X1

(15 percent). The remaining 20 percent went for a variety of smaller programs. According to embassy reports, the Eximbank's management expects future loan commitments to be 80 percent for ship exports, 10 percent for export of industrial plants, and 10 percent for overseas resource investments. [redacted]

***Government Promotion.*** A special import surcharge of 0.35 percent is collected on all imports into Korea with the exception of those destined for the Korean Government or military use or reexport. These funds are then turned over to the Korea Traders Association (KTA), a government-supported business organization, for export promotion. According to the KTA budget, the import surcharge generated some $41 million in 1981. These funds were used to promote small and medium business enterprises, trade fairs, and exhibits as well as to support the Korean Trade Promotion Corporation, the Korean International Economic Institute (a quasi-government research organization), and other market development programs. [redacted]

***Other.*** The Korean export sector is also supported through government-sponsored insurance and guarantees, trading companies, and free export zones. The Eximbank offers export insurance against political and commercial risks. According to embassy reports, this program has grown rapidly, with export coverage swelling from $137 million in 1978 to over $2 billion in 1981. This growth is based primarily on the brisk business Korean construction firms are doing in the Third World; over 90 percent of the insured exports go to less developed countries. To operate this program, the Eximbank receives direct capital infusions from the government, which in 1981 totaled some $25 million. The Eximbank also has a small program offering loan guarantees to domestic banks against losses incurred in financing export sales. [redacted]

In 1975 Seoul began encouraging large Korean trading companies to specialize in the import and export of products. To be accorded General Trading Company (GTC) status, the firm has to have accounted for at least 2 percent of total Korean exports in the previous year. This status conveys benefits beyond those generally available to other exporting firms. [redacted]

[redacted]

[redacted]

The GTCs have been particularly effective in promoting Korean exports. In 1982, 10 firms were designated as GTCs, and their combined sales of $12.5 billion accounted for roughly 58 percent of total Korean exports. By 1983 government planners expect that the GTCs will export 68 percent of total exports. In contrast, they accounted for only 5 percent of total exports in 1975. According to studies published by the Korean Government, this growth has occurred because the GTCs have been particularly effective in seeking out new sales opportunities in foreign markets, negotiating package deals for a wide variety of products, lowering transactions costs, and gathering market information. [redacted]

Korea also offers two free trade zones—the Masan Free Export Zone and the Iri Free Export Zone. To operate in these zones, entrepreneurs must produce exclusively for the export market. In return, the firms are provided with reasonably priced industry infrastructure; exempt from the defense, special consumption, and value-added tax on all imports of raw materials, capital goods, and semifinished goods; exempt from the corporation and property tax for the first five years with a 50-percent reduction for the next three years; allowed to freely import all raw materials and capital equipment needed to manufacture exportable products; and protected from the formation of labor unions. [redacted]

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Taiwan

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## Taiwan

### Overview

According to the published Four-Year Plan for 1982-85, a major objective of Taiwan's trade policy is to widen export product lines and expand trade with countries other than the United States and Japan. In diversifying product lines, government planners have told US officials that they want to move industry into the production of higher technology, higher value-added goods. The government of Taiwan has already developed a major trade link with the Middle East and is cultivating trade relations with a number of East European countries—Czechoslovakia, East Germany, Hungary, Poland, and Yugoslavia. It also has an unofficially sanctioned indirect trade with China.[6] Although Taipei endorses freer trade, it provides a variety of economic incentives to promote the goals outlined in the Four-Year Plan.

### Supporting Policy

***Exchange Rate.*** Although there is strict control over foreign exchange transactions, there are no restrictions affecting trade transactions.

***Import Restrictions.*** Import restrictions have been gradually reduced in recent years. Currently, most imports require an import permit, but, according to trade data, 97 percent of the licenses are freely granted subject to the availability of foreign exchange. The main instrument of control is the customs tariff. Tariff rates range up to 150 percent *ad valorem* and duties are levied on the c.i.f. price plus 15 percent. The tariffs fall primarily on luxury and consumer goods.

***Fiscal Incentives.*** According to official Taiwan reports, Taipei's Statute for Encouragement of Investment provides several incentives for the development and export of capital- and technology-intensive manufactures:

- Export sales are exempt from the business tax.

- Imported raw materials used in exported products are eligible for a rebate ranging from 70 to 100 percent of the duty paid.

- Duties on imported machinery and equipment need not be paid by the following industries: food processing, pulp and paper, rubber processing, petrochemicals, nonmetallic mineral processing, basic metals, machinery, electrical and electronic equipment, transport equipment, ceramics, textiles, construction materials, clinical and surgical instruments, photographic and optical instruments, and precision instruments. 25X1

***Financial Incentives.*** The Export-Import Bank of China (EIBC), a government institution established in 1979, offers supplier and buyer credits as well as fixed-rate relending facilities. The supplier credits, called an Export Loan, are available to Taiwan's 25X1 exporters of capital goods and services. Buyer credits, called a Direct Loan, are available to foreign purchasers of services and capital goods manufactured in Taiwan. The Fixed Rate Relending Facility (FRRF) provides funds to overseas commercial banks, which 25X1 in turn disburse these funds to customers who intend to purchase capital goods from Taiwan. 25X1

According to open government publications, the Export Loan and Direct Loan programs provide for a repayment period of two to seven years from delivery of the manufactured goods or completion of a project. Export Loans are available for 100 percent of the amount of the contract, less a cash downpayment, if the loan is covered by a bank letter of guarantee; otherwise, only 90 percent of the contract amount less 25X1 the cash payment may be financed. The Direct Loan program provides for 100 percent of the contract amount less whatever cash downpayment has been made. A Taiwan content requirement of 50 percent is required of both programs. The Export Loan is available to all manufacturing firms. Trading companies with a three-year record of annual exports exceeding

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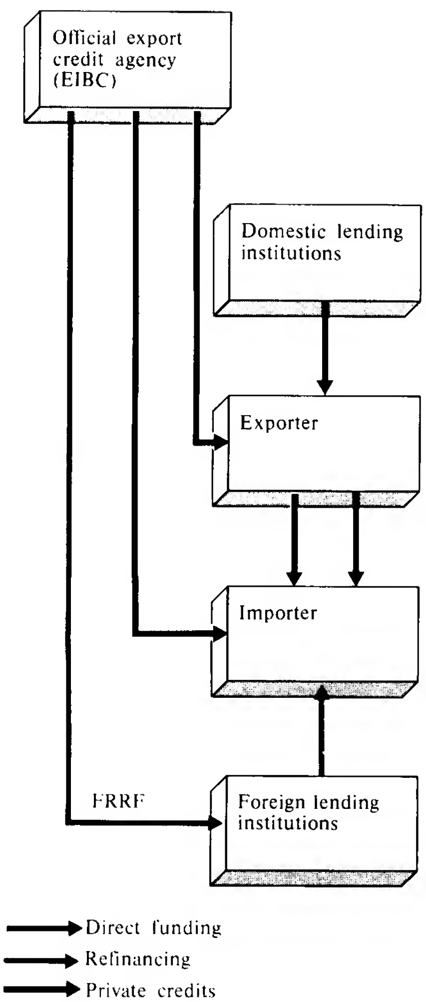
**Figure A-6**
**Taiwan: Flow of Export Financing**

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$3 million are also eligible if they have been designated by a manufacturer to handle a particular export. The Direct Loan program has a minimum transaction requirement of $2 million. As of April 1982 the interest rate for both programs was fixed at 8.5 percent.

**Table A-6**
**Taiwan: Eligible Goods and Repayment Period Under FREF Funding**

| Capital Goods | Maximum Repayment Period *(years)* |
|---|---|
| Freezing machinery | 3 |
| Plastic machinery | 3 |
| Printing machinery | 3 |
| Pump and water supply fittings | 3 |
| Rubber machinery | 3 |
| Shipbuilding | 3 |
| Wood machinery | 3 |
| Agricultural machinery | 5 |
| Casting machinery | 5 |
| Construction and mining machinery | 5 |
| Electric machinery | 5 |
| Food machinery | 5 |
| Machine machinery | 5 |
| Textile machinery | 5 |
| Transport equipment | 5 |
| Boilers | 7 |
| Paper machinery | 7 |
| Chemical machinery | 7 |
| Steel rolling machinery | 7 |

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The FRRF may cover up to 90 percent of an export contract as long as at least 50 percent of the content is of Taiwan origin. Funding may range up to $3 million for any financial institution. As of April 1982 these funds were provided at a fixed interest rate of 8.5 percent. The maximum spread that the relending institution can charge is 1.5 percent. The repayment period may range from two to seven years when the borrower is the end user of the exported products and one to three years when the borrower is a dealer. Only a select group of capital goods is eligible for this funding. These goods, together with the maximum repayment period for each, are presented in table A-6.

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***Government Promotion.*** To enable Taiwan's traders to capitalize on the recovery from the world recession, Taipei's Board of Foreign Trade has been publicly working to:

- Reduce some of the redtape and trade controls that encumber trade administrators.

- Expand the activities of the Taipei World Trade Center Corporation. The government is preparing to begin construction of a world trade center building. It will offer a six-story exhibition center and provide an additional nonofficial channel through which trade may be conducted with countries that lack diplomatic relations with Taiwan.

- Improve Taiwan's trade relations with the United States and Western Europe. Because of the concern that Taiwan's trade surplus with the United States and several European countries could spark protectionist moves, Taiwan trade officials have been sending a stream of procurement missions to "Buy American" and "Buy European."

The Board of Foreign Trade also has been working to concentrate exports in large, more experienced trading companies. According to press accounts, an estimated 50,000 exporters operate in Taiwan. In 1978 the Board established guidelines for the formation of Big Trading Companies, which would become Taiwan's version of Japan's Mitsubishi or Mitsui. They received special incentives such as access to low-interest loans and the right to establish bonded warehouses. According to the press, however, the contribution of the existing five Big Trading Companies has been limited, accounting for under 6 percent of total exports. To further expand their role, they will soon be eligible for the same 25-percent income tax ceiling that applies to manufacturers and will be assigned the role as middlemen between banks and manufacturers seeking credit so that the latter will have greater reason to entrust them with their exports.

***Other.*** The Export-Import Bank of China also provides export insurance and export finance guarantees with its lending facilities. The insurance programs provide medium- and long-term coverage to both commercial banks and exporters against most political and commercial risks. The guarantees are available primarily to assist Taiwan exporters in obtaining commercial bank financing and they cover short-, medium-, and long-term financing needs. An additional guarantee is offered for the export of technology, engineering, and construction services. Insurance premiums are based on credit types and repayment periods. The normal guarantee fee is 1 percent. 25X1

Three export processing zones—Kaohsiung (KEPZ), Nantze (NEPZ), and Taichung (TEPZ)—are operated in Taiwan. Industries located in these zones are exempt from all duties and taxes on imports of machinery, equipment, and materials used in the manufacture of finished products for export. Because of the success of these zones, a new export processing zone is planned. According to embassy reports, the zone would differ from existing export processing zones by eliminating Taipei's foreign currency controls. These changes are designed to make the zone an investment and financial center as well as a manufacturing zone. 25X1

Investors may obtain a similar duty-free status for factories located outside the export processing zones by establishing a bonded enterprise. To qualify as a customs bonded factory, the enterprise must be engaged exclusively in the manufacture of exportable goods and have a paid-up capital of more than NT $5 million (approximately US $140,000). 25X1

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# Appendix B

## Glossary

| | |
|---|---|
| Berne Union | Established in 1934 in Bern, Switzerland, the Union d'Assureurs des Credits Internationeaux has 36 members from 28 countries. It provides for the free exchange of ideas and information and "international acceptance of sound principles of export credit insurance and the establishment and maintenance of discipline in the terms of credit for international trade." |
| Buyer credit | A financial arrangement in which a loan is extended by a bank or export credit agency in the exporter's country to the foreign buyer or bank in the buyer's country. These credits have relatively long repayment periods, generally over five years, and are widely used to finance exports of capital goods. |
| Consensus | Also commonly called the OECD Consensus or Arrangement. An unsigned agreement in February 1976 between Canada, France, West Germany, Italy, Japan, the United Kingdom, and the United States establishing guidelines for officially supported export credits. It has been revised several times. |
| Discounting | The sale by a commercial bank of an obligation it has purchased from an exporter, at a discount, to a central bank or export credit agency. |
| Export credit agency | A governmental, semigovernmental, or private agency facilitating exports through insurance, guarantees, direct funding, or funding support. |
| Export processing zone | An industrial zone, often situated near a port or airport and sometimes operating as a free trade zone, that is supplied with the necessary infrastructure facilities and investment incentives to encourage foreign and domestic entrepreneurs to establish a modern manufacturing complex, which is used for the production of exportable products. |
| Funding | This term includes a wide range of direct funding programs with interest rates subsidized or supported by export credit agencies. A distinction is drawn between these direct funding programs and those where commercial banks discount exporter obligations at favorable rates or receive favorable rate refinancing, which they pass along for export transactions. |
| Free trade zone | Designated areas generally near a seaport or airport into which goods from abroad can be brought without quota restrictions or the payment of tariffs and excise taxes. The goods are not subject to exchange controls or the majority of statistical reporting requirements and regulations aimed at the protection of consumers. |
| Guarantee | An assurance provided by an export credit agency to a third party, most often a bank providing financing, that in the event of nonpayment or noncompliance by the creditor or exporter, the agency will pay the third party's premiums. |

| | |
|---|---|
| Insurance | A contract administered by a public agency or private company acting on behalf of the public sector that protects the exporter against the loss of payment caused by commercial or political factors in the importing country. |
| Interest rate equalization | An export credit program that provides a commercial bank the difference between the subsidized interest rate payable on the bank's supported export loan and the bank's market cost of funds plus an agreed-upon interest spread. |
| Refinancing | Funding provided by an export credit agency to a commercial bank to assure liquidity and thereby enable the bank to finance export transactions. Generally, this funding is extended to an overseas bank that in turn lends to its customers to finance the purchase of goods and services from exporters in the country of the export credit agency. |
| Supplier credit | A financial arrangement in which the supplier (exporter) extends credit to a foreign buyer to finance purchases. Credit terms are typically extended up to five years. These credits are normally used to finance all manufactured exports except capital goods. |
| Trading company | A firm authorized by the government to conduct the import and export transactions of the industrial sector. These firms tend to specialize in product or service lines and receive special fiscal and financial incentives that improve their profitability and promote the country's trade. |

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